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February 8, 2002

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

Ex Parte

William Caton
Office of the Secretary
Federal Communications Commission
445 12th Street, SW
Washington, D.C. 20554

REDACTED – FOR PUBLIC INSPECTION

Re: *Application by Verizon New England Inc. et al. to Provide In-Region
InterLATA Services in Rhode Island*
CC Docket No. 01-324

Dear Mr. Caton:

Enclosed for filing please find ex parte letter of AT&T Corp. ("AT&T") in connection with the above referenced matter. AT&T is submitting the original and two (2) copies of its ex parte and supporting exhibits in redacted form.

AT&T is also submitting under seal the portions of its ex parte that contain material designated as confidential pursuant to the Protective Order in this matter. These pages bear a legend indicating that they are confidential.

Please let me know if any additional information is required. Thank you.

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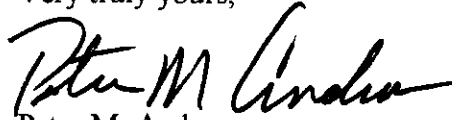
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Magalie Roman Salas

January 14, 2002

Page 2

Very truly yours,

A handwritten signature in black ink, appearing to read "Peter M. Andros". The signature is fluid and cursive, with the first name "Peter" and last name "Andros" clearly distinguishable.

Peter M. Andros

Legal Assistant

Encl.

cc: Michael Powell, Chairman
Kyle Dixon
Kathleen Abernathy, Commissioner
Matthew Brill
Michael Copps, Commissioner
Jordan Goldstein
Kevin Martin, Commissioner
Sam Feder
Linda Kinney
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February 8, 2002

By Hand Delivery

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
445 12th St., S.W.
Washington, DC 20554

Re: *Application by Verizon-New England for Authorization to Provide In-Region InterLATA Services in the State of Rhode Island, CC Docket No. 01-324.*

Dear Mr. Caton:

At the request of the Commission's staff, AT&T submits this *ex parte* letter and the attached supplemental declaration of Michael I. Lieberman to respond to the arguments on the issue of "price squeeze" that Verizon advanced in its Reply Comments.

Preliminarily, the Commission obviously need not reach the price squeeze question if it concludes that Verizon's Rhode Island UNE rates do not comply with TELRIC and thus are not "cost-based." AT&T's Comments and Reply Comments demonstrated that no such finding can be made, and in its *ex parte* letter dated February 1, 2002, AT&T demonstrated that the January 28, 2002, Order of the New York Public Service Commission has foreclosed the only ground on which Verizon even attempted to justify its switching and other UNE rates under TELRIC: Verizon's claim that the Rhode Island rates are comparable to rates found to satisfy

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TELRIC in New York. The NYPSC Order establishes that Rhode Island switching rates are three times higher than what TELRIC now requires in New York.

However, even if the Commission could somehow deem the Rhode Island UNE rates to fall at the high end of a “range” of TELRIC rates, AT&T previously demonstrated that these “high end” UNE rates foreclose any firm from profitably using UNE-P to provide retail residential service in Rhode Island and that they effect a classic “price-cost squeeze” that requires denial of the application. AT&T Comments, Declaration of Michael I. Lieberman at 3-9; AT&T Reply Comments at 4-10. While Verizon has objected to AT&T’s showing on both legal and factual grounds, its objections are meritless.

Verizon’s Legal Claims. Verizon’s primary claim is that it is legally irrelevant that UNE-P purchasers cannot economically provide service under Verizon’s existing UNE rates in Rhode Island. Verizon Reply Comment at 21-24. Verizon relies on antitrust cases that purportedly hold that a price squeeze can exist only if “essential inputs” are not available at a “fair price.” Verizon claims that this standard cannot be met here because UNE prices are necessarily “fair” if they have been found to fall within the range that satisfies TELRIC. In all events, Verizon claims that the UNE platform (“UNE-P”) “is in no way an essential input” because the Act makes available resale under § 251(c)(4) and “a variety of other means in which to gain access to Verizon’s network” (*id.* at 21) and because Cox is purportedly offering residential local telephone service over its cable television systems to between 75 and 95% of the home in Rhode Island. *Id.* at 22. These claims are baseless.

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As an initial matter, Verizon misstates the applicable antitrust decisions. *Alcoa* holds that a firm with monopoly control over an input essential to the provision of a finished product is not charging a “fair” input price and is engaged in a price squeeze if purchasers of the input cannot make a “living profit” from sale of the finished product at the incumbent’s retail prices – as purchasers of UNEs plainly cannot in Rhode Island. *United States v. Aluminum Co. of America*, 148 F.2d 416, 436-38 (2d Cir. 1945). In *Town of Concord v. Boston Edison*, 915 F.2d 17 (1st Cir. 1990), the court held that allegations that electric utilities have set wholesale rates to effect a price squeeze “generally” will not state claims under the antitrust laws because, among other things, the governing regulatory statute requires FERC to determine if a price squeeze will result at the time it reviews the lawfulness of the utility’s wholesale rates. *Id.* at 28.

The antitrust decisions are simply besides the point here for a similar reason. Whether or not Verizon is also violating the antitrust laws, § 271 bars the Commission from granting Verizon long distance authority unless the Commission finds (1) that the UNE rates are “nondiscriminatory” as well as cost-based (§§ 252(d)(1), 271(c)(2)(B)(ii) & (d)(3)(A)) and (2) that the grant of the application is in the “public interest.” § 271(d)(3)(C). If the available revenues from the provision of residential services are insufficient to cover the wholesale costs of the UNEs (and the firm’s internal retail costs), this fact establishes both that checklist item two has not been met and that a grant of the application is not in the public interest. The Commission thus cannot lawfully grant a § 271 application unless it addresses claims that firms cannot economically provide residential service at existing UNE and retail rates.

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Discrimination And Checklist Item Two. To satisfy checklist item two, a BOC must prove that its UNE rates are not only cost-based, but also are “nondiscriminatory.” §§ 252(d)(1) & 271(c)(2)(B)(ii). The Supreme Court has held that even if a utility’s wholesale rates are within the range of reasonable cost-based rates, the rates are nevertheless “discriminatory” and “anticompetitive” if they fall at the high end of that range and they preclude wholesale purchasers from economically competing with the utility’s retail services to any class of customers. *FPC v. Conway Corp.*, 426 U.S. 271, 278-79 (1976). The resulting price squeeze establishes that the utility is discriminating by charging “high-end” rates to its wholesale customers but imputing “low-end” wholesale rates to its own retail operations. *Id.*

Here, there is no question that if Verizon’s UNE rates could somehow be found to be cost-based, it could only be on the theory that they fall at the high end of a range of rates that are reasonable under TELRIC. If these high-end UNE rates foreclose UNE purchasers from economically providing residential competition, then the Supreme Court’s decision in *Conway* establishes that Verizon is engaged in “discrimination,” and it has not satisfied checklist item two even if the UNE rates can be deemed to be cost-based. It necessarily follows that Verizon may not satisfy this checklist item unless it reduces its UNE rates to the low end of the TELRIC range.

Verizon’s arguments about the availability of resale and the existence of a cable television-based competitor are simply irrelevant if Verizon’s high end UNE rates effect a price squeeze and Verizon is thus engaged in discrimination that violates checklist item two. When

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the checklist is not met, § 271(d)(3) requires that the application must be denied, irrespective of any other factors.¹

Public Interest. In addition, if there is an insufficient margin to allow UNE purchasers to offer residential service for these or any other reasons,² the D.C. Circuit has expressly held that this is a factor that can establish that the grant of the application is not in the public interest. *Sprint Communications Co. v. FCC*, 274 F.3d 549 (D.C. Cir. 2001). In particular, the Court remanded the Commission's decision to grant SBC authority to provide long distance service in Kansas and Oklahoma because the FCC had not addressed the merits of AT&T's and WorldCom's showings that SBC's UNE rates had effected such a price squeeze in Kansas and in Oklahoma. *Id.* at 553-55.

The D.C. Circuit reasoned that a finding of whether such a price squeeze exists is at the very heart of the public interest determination required by § 271. Indeed, it noted that, in contrast to the provisions of the Federal Power Act that were at issue in *Conway*, § 271 of the Act "aims directly at stimulating competition," for its whole point is to assure that local competition is legally and economically possible before a BOC receives long distance authority

¹ In *Sprint Communication Co. v. FCC*, 274 F.3d 549 (D.C. Cir. 2001), the Court did not address the question of whether a price squeeze that results from the charging of "high end" UNE rates establishes discrimination that precludes a finding a compliance with checklist item two – presumably because appellants had not presented that claim to the Commission in the Kansas-Oklahoma § 271 proceedings. See 47 U.S.C. § 405. However, the issue has been squarely raised in this proceeding, and it will be reversible error for the Commission to find checklist compliance if it does not address the evidence of a price squeeze on the merits.

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in a state. 274 F.3d at 555. In this regard, the D.C. Circuit had previously held that the “premise” of the MFJ’s interexchange services restriction is that a BOC that “enjoyed a monopoly on local calls” would “ineluctably leverage that bottleneck control in the interexchange (long distance) market” (*United States v. Western Electric Co.*, 969 F.2d 1231, 1238 (D.C. Cir. 1992)), and the D.C. Circuit has expressly held that Congress adopted § 271 on the basis of the MFJ’s antitrust “findings” that a BOC must be excluded from long distance services until long distance carriers have the practical ability to compete in providing exchange and exchange access services to customers in that state. *BellSouth v. FCC*, 162 F.3d 678, 689 (D.C. Cir. 1998). *Id.* The reality is that if competition is economically impossible for residential customers, a BOC that received long distance authority will monopolize the business of customers who want to obtain local and long distance service from a single source, and the BOCs will have anticompetitive advantages in obtaining long distance business from other customers. *AT&T v. Ameritech*, 13 F.C.C.R. 21438, ¶¶ 5, 39 (1998), *aff’d sub nom. U S West v. FCC*, 177 F.3d 1057 (D.C. Cir. 1999).

That is why the Commission’s prior decisions hold that § 271 requires not just that it consider if the checklist is met, but also that it apply the public interest prong to “ensure that no other relevant factors exist that would frustrate the congressional intent that local markets are open to competition” before long distance authority can be granted. *Kansas-Oklahoma Order*, ¶ 267; *accord NY Order*, ¶ 423; *Texas Order*, ¶ 417. That is why *Sprint* held that the

² *E.g.* if UNE rates were at the low end of the range of reasonableness but Verizon were charging below-cost residential rates and were not sharing universal service subsidies with UNE-P

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objects of § 271 require the Commission to determine if UNE-P purchasers can receive sufficient margins to make residential competition economic under the public interest prong.

However, Verizon relies on two different grounds to argue that an application can be in the public interest even if UNE-P cannot be economically used to serve residential customers. Each is baseless.

Resale And UNE-L. First, Verizon notes that there are other entry vehicles available to long distance carriers, and it specifically identifies resale under § 251(c)(4). Verizon Reply Comments at 21-22. But resale is irrelevant for this purpose. The wholesale discount that has been set in Rhode Island is wholly insufficient to allow any firm to cover its internal costs of service, and no firm could economically provide broad-based local exchange service in Rhode Island through resale. *See Supplemental Lieberman Decl.* ¶ 18.

More fundamentally, resale would be irrelevant even if the wholesale discount that has been set in Rhode Island was sufficient, for resale does not give a CLEC access to the “inputs” required to provide long distance service. In particular, firms engaged in resale are entitled to use the BOCs’ facilities to provide only exchange service and not exchange access service. *See Local Competition*, 11 F.C.C.R. 15499, ¶ 873 (1996). Resale thus has no effect on the BOCs’ monopoly over the exchange access services that originate and terminate all long distance calls, and resale cannot eliminate a BOC’s ability to leverage its exchange access monopoly into the long distance market. In this regard, it is ironic that Verizon would here rely

purchasers.

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on the fact that “the Commission’s own lawyer” had advanced this contention at oral argument in *Sprint Communications Corp. v. FCC*. Verizon Reply Comments, p. 22 n. 27. For when the Commission’s counsel did so, AT&T’s counsel pointed out that resale cannot be used to provide exchange access, and the Court told the Commission’s counsel that unless he could dispute that fact – as he could not – resale could not be relied on to defeat the price-squeeze claim. Tr. of Oral Argument, *Sprint Communication Corp. v. FCC*, No. 01-1076 pp. 42-46 (D.C. Cir. September 17, 2002).

Nor is there any other entry vehicle that could allow AT&T and multiple other CLECs to provide exchange and exchange access in connection with residential service throughout Rhode Island. In this regard, the only theoretical alternative to UNE-P would be an arrangement in which firms would attempt to provide residential service by leasing unbundled loops from Verizon and combining them with CLEC switches to provide service. However, such a “UNE-L” strategy is now wholly uneconomic for this purpose in Rhode Island (and elsewhere). Quite apart from the fact that carriers cannot rationally invest in switches until they have used UNE-P to build up a customer base (*UNE Remand Order*, 15 F.C.C.R. 3696, ¶ 260 (1999)), Verizon and other BOCs have not deployed technology that allows a customer electronically to change from one local exchange carrier to another at no or little cost. Instead, these changes require manual “hot cuts” which are expensive and which have proven impossible to administer without causing unacceptable levels of service outages even when UNE-L is used only for low volumes of orders for business customers. *See Supplemental Decl.*, ¶¶ 19-20.

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Residential Service Over Cox's Cable TV Systems. Second, Verizon argues that the fact that Cox is offering facilities-based local telephone service eliminates any basis for assessing the UNE price squeeze claim under the public interest prong of § 271. In Verizon's view, Cox's offering means that "there is a ubiquitous alternative to Verizon's network" (Verizon Reply Comments, p. 22) and that "the policy for promoting UNE-based competition in the first place already has been fulfilled." *Id.* at 23.

These claims are baseless – even apart from the fact that Cox is actually now serving only a minute fraction of the residential lines in Rhode Island. Cox does not offer unbundled network elements to CLECs, and Verizon cannot and does not claim that competition from Cox has caused Verizon to reduce its UNE rates to the level that would prevail in a competitive market. At best, Cox's offering simply means that the monopoly that Verizon now enjoys over end-to-end local services could evolve into a duopoly over time. Accordingly, if Verizon could obtain long distance authority with its current UNE rates, the consequence would be that today's intensely competitive long distance market in Rhode Island would be transformed into one in which there would be, at best, a duopoly over the residential customers who desire one stop shopping for local and long distance service, and in which Verizon and Cox would have unfair and anticompetitive advantages in providing long distance services. That would be antithetical to the Act and to the public interest.

Indeed, the Commission has expressly rejected the precise claim that Verizon here advances and has held that the existence of a single cable television-based

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competitor in no way undermines the necessity of assuring that multiple firms can provide broad-based residential services by leasing UNEs at rates that allow them economically to offer exchange and exchange access services for these customers. The Commission has noted that “although Congress fully expected cable companies to enter the local exchange market using their own facilities,” Congress “still contemplated that incumbent LECs would be required to offer [UNEs] to requesting carriers.” *UNE Remand Order*, 15 F.C.C.R. 3695, ¶ 55 (1999). It concluded that a “standard that would be satisfied by the existence of a single competitive LEC using a non-incumbent LEC element . . . would be inconsistent with the Act’s goal of creating robust competition in telecommunications,” for that “would not create competition among multiple providers of local service that would drive prices to competitive levels.” *Id.* Instead, it would “create stagnant duopolies comprised of the incumbent LEC and the first new entrant in a particular market.” *Id.*; *see also id.* ¶ 189.

The Commission’s prior holdings have particular significance in the context of decisions on applications for long distance authority. There is no question that, if this application is granted, Verizon will have overwhelming market power throughout Rhode Island unless multiple firms can economically offer competing local services by leasing UNEs. That is the very reason. Indeed, Congress made it explicit that it would be premature to grant long distance authority before it is economically possible to develop such statewide local competition, because that would risk damaging the already competitive long distance market. 141 Cong. Rec. S8464 (June 15, 1995) (Statement by Sen. Dorgan) (allowing BOC entry “prematurely. . . risk[ed] damaging that competitive [long] distance market.”); 141 Cong. Rec. S8134 (June 12,

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1995) (statement of Sen. Kerry) ("Removing the separation between the local markets and other markets without ensuring that the Bell Companies cannot use the local monopoly to hurt competition and long-distance could squander the gains of the past decade"); 142 Cong. Rec. S688 (daily ed. Feb. 1, 1996) (statement of Sen. Hollings) ("The basic thrust of the bill is clear: competition is the best regulator of the marketplace. Until that competition exists, monopoly providers of services must not be able to exploit their monopoly power to the consumer's disadvantage . . . Telecommunications services should be deregulated after, not before, markets become competitive."); *accord*, 142 Cong. Rec. E204 (Feb. 23, 1996) (statement of Rep. Forbes). It would wholly defeat the objects of § 271 and be squarely contrary to the public interest to allow Verizon to provide long distance service in a state in which there is no economic possibility that AT&T, WorldCom, and other long distance carriers could offer residential exchange and exchange access services throughout the state and in which the only competition to Verizon's packages of local and long distance service would be that provided by a single cable television operator.

Factual Claims. Verizon also cursorily argues, in the alternative, that the profit margin analysis that AT&T offered in its opening comments through the Lieberman Declaration "is flawed as a factual matter." Verizon Reply Comments, p. 25 & Dupelo, Garzillo, & Anglin Reply Declaration, ¶¶ 28-29 & Attachment 2. In particular, Verizon claims that Mr. Lieberman improperly ignored the revenues that AT&T could earn from the Subscriber Line Charge, from access charges, and from intraLATA toll services and that when these revenues are included, the profit margin is positive. *Id.* In this connection, Verizon and the Rhode Island Public Utilities

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Commission ("RI-PUC") assert that the proper comparison is between the costs of the UNE platform and the \$28.95 in monthly charges for Verizon's Unlimited Local Calling Option that covers all these services. *Id.*; RI-PUC Reply Comments at 45.

These claims too are meritless, as explained in detail in the attached Supplemental Declaration of Michael Lieberman. But three points deserve mention.

First, the revenues that can be earned from Verizon's Unlimited Local Calling Option are not pertinent to this analysis. This is an offering that is targeted to high-end residential customers with high volumes of usage and enhanced needs for features. The proper comparison is with the revenues that the *average* residential customer generates at existing retail and access rates, and the fact is that the average residential customer revenues in Rhode Island do not even cover the average costs of the UNEs that comprise the platform, as weighted to the three density zones, much less the internal costs of any CLEC. If these average revenue figures are used – as they must be – there is no question that statewide residential entry through UNE-P is unprofitable. *See* Supplemental Lieberman Decl. ¶¶ 4-6.

Second, AT&T's prior profit margin analysis fully reflected the revenues that can be earned from the Subscriber Line Charge and from exchange access services. It did not, however, include intraLATA toll revenues, for intraLATA toll is provided in a separate market from local services, and intraLATA toll is a service that AT&T is now providing in Rhode Island independently of any decision whether to offer local service. As the Commission has held in another context, a carrier should not be forced to enter one market in order to be able to enter

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another. *Line Sharing Order*, 14 FCC Rcd. 20912, ¶ 56 (1999) (firms that wish to provide DSL should not also be required to provide voice services); *see also* Brief of FCC, *USTA v. FCC*, No. 00-1012, p. 27 (filed Sept. 14, 2001).

But this issue need not be reached here. IntraLATA toll is irrelevant to any margin analysis in Rhode Island. The Rhode Island PUC has already eliminated toll charges for most of intraLATA calls for which these charges were formerly assessed, and Rhode Island is considering eliminating toll charges for the remainder of such calls. *See* Supplemental Lieberman Decl., ¶ 5. No CLEC could rationally make entry decisions in this state on the premise that a revenue stream from intraLATA toll calls could continue over the long term.

In all events, the profit margins would be negative for UNE purchasers in Rhode Island even if all of the net revenues that can now be earned from the provision of intraLATA toll are counted in the analysis. *See* Supplemental Lieberman Decl., ¶ 6.

Third, AT&T's prior margin analysis provided specific numbers for each category of revenues and costs and explained how the revenues and costs were derived and the applicable sources of its data.³ The margin analysis in Verizon's Reply Comments, in contrast, is based on figures that were pulled out of thin air, that are lumped together in undefined "other" categories, and that have no identified sources. If Verizon or any other BOC is to criticize an AT&T profit analysis by advancing different figures for any subcategory of revenues or costs, they must be

³ Since that analysis was prepared, AT&T has obtained other data that show that the prior analysis actually overstated the profitability of entry through UNE-P in Rhode Island. *See* Lieberman Suppl. Decl. ¶¶ 21-25.

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required to explain why AT&T's figure is wrong and what the source is for their new number. Here, however, Verizon has offered only a cursory one page attachment with no explanations whatsoever.

For all these reasons, even if the Commission were to find that Verizon's Rhode Island UNE rates are within the range of cost-based rates, it would be required to reject the application on the grounds that (1) because the high-end UNE rates effect a price squeeze, they are "discriminatory" and checklist item two has not been met and (2) in all events, the price squeeze means that the application is not in the public interest.

Sincerely,

A handwritten signature in black ink, appearing to read "Peter D. Keisler", written in a cursive style.

Peter D. Keisler

Attachment

**BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554**

In the Matter of)	
)	
Application by Verizon New England Inc.,)	
Bell Atlantic Communications, Inc. (d/b/a)	CC Docket No. 01-324
Verizon Long Distance), NYNEX Long)	
Distance Company (d/b/a Verizon)	
Enterprise Solutions), Verizon Global)	
Networks Inc., and Verizon Select Services)	
Inc., for Authorization To Provide In-)	
Region, InterLATA Services in Rhode)	
Island.)	

**SUPPLEMENTAL DECLARATION OF MICHAEL LIEBERMAN
ON BEHALF OF AT&T CORP.**

I. BACKGROUND AND SUMMARY

1. My name is Michael R. Lieberman. I am the same Michael R. Lieberman who filed a declaration with AT&T's initial comments in this proceeding. In that declaration, I demonstrated, among other things, that Verizon's inflated UNE rates make it uneconomic for purchasers of the UNE-platform to provide residential service in Rhode Island. In particular, I demonstrated that even if potential new entrants had no internal costs of entry – *e.g.*, marketing, customer service, billing, order processing, and other operating activities – the margins (revenues minus costs) available to new entrants in Rhode Island would be *negative* or *de minimis* in all UNE rate zones. And the statewide average residential margins are *negative*.

2. The purpose of my supplemental testimony is to respond to the criticisms of my margin analysis by Verizon's witnesses, and to explain why the alternative "margin"

analysis submitted by those witnesses cannot be relied upon.¹ I also demonstrate that Verizon's assertion that resale and facilities-based entry in Rhode Island is economically feasible for new entrants is wrong. Lastly, I update my December 17, 2001 margin analysis to reflect new information and certain improvements. *See* Exhibits A1 – A9.

II. VERIZON'S CRITICISMS OF MY MARGIN ANALYSIS ARE BASELESS.

3. Verizon asserts that my margin analysis fails to account for revenues obtained from the subscriber line charge ("SLC") and access charges. *CGA Decl.* ¶ 29. That assertion is plainly false. Paragraph 17 of my initial declarations states that "[t]he federal Subscriber Line Charge brings in an additional \$5.00/line/month [in revenues]." And Exhibit 3 to my initial declaration shows that the SLC is included in my margin calculations. Similarly, paragraph 18 of my initial declaration explains how I computed access revenues, and Exhibit 3 to my initial declaration shows that those access revenues are accounted for in my margin analysis.

4. Verizon also asserts that my margin analysis is inaccurate because it fails to reflect IntraLATA toll revenues. *CGA Decl.* ¶ 29. But, IntraLATA services can be provided by carriers – and in many cases are already provided by carriers – without entering Rhode Island's local telephone markets. Accordingly, revenues from those services are not properly attributable to local telephone entry and are not relevant to the determination of whether revenues associated with entry into the local telephone market would exceed the costs of that entry by a sufficient margin to make local entry economically viable.

5. Verizon's IntraLATA toll argument is also wrong. The Rhode Island Public Utilities Commission has already eliminated toll charges for many of its intraLATA calls

¹ *See* Reply Declaration of Donna C. Cupelo, Patrick A. Garzillo, and Michael J. Anglin ("*CGA*

for which these charges were formerly assessed, and is considering eliminating toll charges for the remainder of such calls. For example, calls that originate from outside of Providence, Rhode Island and that terminate within Providence no longer incur a toll charge.² Furthermore, even aside from the Rhode Island PUC's actions, analysis of Verizon's ARMIS data shows that IntraLATA toll revenues have been declining at an average rate of 10% each year since 1997. *See Exhibit A-10.* As a result of the Rhode Island PUC actions and the natural decline in toll revenues, potential local entrants in Rhode Island cannot rationally make entry decisions that rely on a revenue stream from IntraLATA toll revenues over the long term.

6. In all events, this issue is moot. Adding IntraLATA toll revenues to the Rhode Island margin analysis would not change the fact that statewide margins in Rhode Island are negative. Even today, accounting for potential IntraLATA toll revenues that may be available to new entrants in Rhode Island (depending on Rhode Island PUC action) would increase the margin by only ***. ***. Adding that amount to my margin analysis still results in *negative* or miniscule margins in all UNE zones, and a statewide average margin of *negative* ***. ***.

III. VERIZON'S MARGIN ANALYSIS IS WRONG AND UNDOCUMENTED.

7. AT&T, WorldCom and ASCENT all demonstrated in their initial comments that Verizon's Rhode Island UNE rates resulted in a price squeeze that precluded profitable local residential entry in Rhode Island. *See AT&T at 17; WorldCom at 3, n.2;*

Decl.”).

² *See State of Rhode Island And Providence Plantations Public Utilities Commission, Bell Atlantic – Rhode Island Compliance Filing on Expanded Local Calling Areas, Report and Order, Docket No. 2912 (October 15, 1999).*

ASCENT at 4. In an attempt to rebut these showings, Verizon filed its own “margin analyses” that, according to Verizon, demonstrates that residential UNE-platform entry would be economically feasible in Rhode Island. *See CGA Decl.*, Att. 2. Verizon’s purported margin analyses should be given no weight.

8. Verizon actually provides two margin analyses: (1) an “average customer” analysis and (2) a “Local Package” margin analysis. The “Local Package” analysis is irrelevant here. The “Local Package” offering is a feature-rich premium service that costs over \$10.00 more than Verizon’s basic package. That means that Verizon’s “Local Package” margin analysis would be correct only for a new entrant that could seek out and serve only that minority of Rhode Island customers who would purchase that premium package. But a new entrant considering entry would recognize that not all customers will be above average. Rather, as in any business, *average* revenues must cover average costs. Moreover, focusing only on high value customers who could (and would) purchase the more expensive “Local Package” service or its CLEC equivalent would contravene the public interest. All Rhode Island customers should enjoy the benefits from competition, not just those who are able to (and choose to) purchase premium services. In any event, the targeted service offering that Verizon’s “Local Package” service offering analysis assumes could not practically be implemented in the long run both because all new entrants would be relegated to competing for that sliver of the market and because Verizon could respond simply by offering greater discounts on that particular bundle of services.

9. Verizon’s “Average Customer” analysis is also not probative because it does not support Verizon’s assertion that UNE-P entry in Rhode Island is economically feasible. Even with Verizon’s severely inflated “Average Customer” margins, Verizon’s analysis shows

that entrants could earn only *** /line/month in Rhode Island, which is not sufficient to cover entrants' internal costs of providing service in Rhode Island.³

10. In any event, Verizon's analysis is riddled with unsupported assertions, as well as fundamental methodological errors and incorrect data and assumptions.

11. *"Other" Categories.* Both the revenue and cost assumptions in Verizon's "margin analysis" include a category labeled "other." Verizon does not even attempt to explain what these "other" line items represent, let alone how they were developed. For example, Verizon's revenue estimate contains an unexplained *** line item titled "Other (Features, etc)." As I demonstrate (and fully document) in Exhibit A-1, Rhode Island entrants can expect to receive \$3.57 in feature revenues.⁴ Apparently, the remaining *** (*** - \$3.57) falls within the categories that Verizon has mysteriously labeled "other" and "etc." See *CGA Decl.*, Att. 2. While I naturally cannot know what this mysterious other category is intended to include, I am aware of no "other" average revenues that can be earned and that are properly attributable to the provision of local exchange and exchange access services for or in connection with residential service.

12. *Revenue Calculation Errors.* First, Verizon's margin analysis assumes that entrants will receive *** /line/month in access revenues from the provision of

³ As explained in my initial declaration, and as confirmed by WorldCom, entrants' internal costs are at least \$10. See WorldCom Corrected Reply Comments, *Re: CC Docket No. 01-138 Application by Verizon for Authorization to Provide In-Region, InterLATA Services in Pennsylvania*, Declaration of Vijetha Huffman at page 3 (August 7, 2001); see also WorldCom Comments, *Verizon New Jersey 271 Application*, CC Docket No. 01-347, Declaration of Vijetha Huffman (Filed January 14, 2002) (explaining why internal costs exceed \$10.00).

⁴ I also provided a full explanation of the development of feature revenues in my initial declaration (¶ 17).

UNE-platform services in Rhode Island. *CGA Decl.*, Att. 2. I estimate that these access revenues are inflated by ***. ***. See Exhibit A-7 (attached) (showing derivation of access revenues of \$1.24). Of course, it is impossible to determine exactly why Verizon's access revenue calculation is so inflated because Verizon has not provided any information as to how it developed its access revenue estimate.

13. Second, Verizon's margin analysis incorrectly includes toll revenues of ***. ***. As explained above, toll revenues are not properly attributable to local telephone service and, therefore, are not relevant to a determination of whether the revenues associated with entry into the local telephone market in Rhode Island would exceed the costs of that entry by a sufficient margin to make such entry profitable. In any event, as described above, even if toll revenues were relevant they would be much lower than the undocumented ***. *** reflected in Verizon's "analysis." One reason why Verizon's toll revenues appear inflated may be that Verizon improperly included business revenues in its calculation of local residential toll revenues.⁵ That error would substantially inflate toll revenue estimates because, as the Commission has recognized, average business toll usage per line is far higher than average residential-only toll usage per line.⁶ Moreover, to the extent that toll revenues should be included at all, the relevant revenues are the toll revenues net of the costs of providing InterLATA toll services. Because Verizon's analyses provides no documentation, it is impossible to determine if Verizon computed toll revenues in this way.

⁵ As shown in Exhibit A-10, Verizon's toll revenues appear to be very close to those for residential and business lines.

⁶ The Commission's Synthesis Model, for example, assumes that that per line business Intrastate toll minutes of use are two times the residential per line toll minutes of use.

14. Third, Verizon's "local/SLC" category is overstated. Current Rhode Island SLC rates are \$5.00/line/month. *See* Exhibit A-1. My estimate of the average basic local service rate in Rhode Island is \$16.10/line/month. *See id.* Therefore, the total local plus SLC revenues that would be available to entrants in Rhode Island is \$21.10, not ***⁷, as Verizon asserts. Verizon offers no explanation of its inflated local/SLC revenue estimate.⁷

15. *Cost Calculation Errors.* Verizon's cost analysis includes a "Loop" cost that is understated. As shown in Exhibit A-1, the average cost of a loop in Rhode Island (weighted by zone) is \$14.14. Verizon, however, has computed the cost of a loop in Rhode Island to be only ***. It appears that Verizon's understatement of residential loop costs is due to the inclusion of business lines in its calculations, which, due to a different line mix across zones, have a lower average cost than residential loop costs. Again, however, Verizon does not actually explain how it derived its understated loop costs.

16. Thus, Verizon's Rhode Island margin analyses are both unsupported and unreliable and the Commission cannot reasonably rely upon them to support this application.

IV. RESALE AND UNE-L ENTRY IN RHODE ISLAND ARE NOT FEASIBLE ENTRY ALTERNATIVES FOR NEW ENTRANTS.

17. Verizon claims that the fact that its UNE-platform rates preclude residential entry is irrelevant because potential competitors have other modes of entry available to them. According to Verizon, even without the UNE-platform, it would still be economically feasible for entrants to provide local residential services in Rhode Island through resale or a UNE-loop facilities-based approach. Verizon is again wrong.

⁷ Notably, Verizon's local/SLC revenue estimate is even higher than that which is available in

18. *Resale.* In Rhode Island, entrants can purchase residential lines from Verizon at a 19.04% discount from the retail rates for those lines. The average retail revenue for a line in Rhode Island is about \$19.67. That means that a local entrant in Rhode Island can purchase those lines for resale for \$15.92. The margin that is available to local residential resale entrants in Rhode Island is the difference between the retail rate for that line and the discounted rate for that line, *i.e.*, $\$19.67 - \$15.92 = \$3.75$.⁸ That margin does not even come close to covering the entrant's \$10.00+ internal costs of providing those services. Thus, resale is not an economically feasible alternative to UNE-P for provision of local exchange services to residential customers.

19. *UNE-Loop.* The only facilities-based alternative to UNE-platform in Rhode Island would be a UNE-loop strategy in which entrants attempt to provide residential service by leasing unbundled loops from Verizon and combining them with the entrants' own switches to provide local residential service. The costs and administrative difficulties of such an entry strategy, however, make UNE-loop entry economically infeasible for new entrants. In its *UNE Remand Order* (§§ 254-258),⁹ the Commission itself recognized that entrants cannot rationally invest in switches until they have used UNE-P to build up a customer base. As discussed above, Rhode Island entrants cannot build up such a customer base because Verizon's Rhode Island UNE rates preclude profitable UNE-platform entry.

Verizon's most expensive local rate zone. In that rate zone local service is \$17.26. Therefore, the local/SLC revenues would sum to only \$22.26.

⁸ Unlike UNE-P entrants, resellers do not receive SLC revenues and also cannot generate access revenues (or savings) from exchange access service.

⁹ *Implementation of the Local Competition Provisions of the Telecommunications Act of 1996*, Third Report and Order, 15 FCC Rcd. 3696, § 260 (1999); *see also Implementation of the Local*

20. More fundamentally, entrants could not rationally enter Rhode Island with a UNE-loop based strategy because the costs of provisioning UNE-loop and connecting them to entrants' switches make mass-market residential UNE-loop entry economically infeasible.¹⁰ Verizon has not deployed a technology that allows customers to change electronically from one local exchange carrier (e.g., Verizon) to another local exchange carrier (e.g., a new entrant) at no or minimal cost. Instead, the change requires entrants to purchase a "hot cut." Even if, contrary to prior experience, hot cuts could be performed in mass-market volumes and were performed in a timely manner so they did not cause outages for substantial numbers of customers, the hot cut charges for each new customer, combined with additional collocation and transport costs that the ILEC does not incur, make a UNE-loop strategy, at best, only economic for business customers, not for residential customers.¹¹ That is especially true because the substantial turn-over (or "churn") rate associated with the provisioning of competitive local residential services can make it impossible for carriers to recover their up-front costs of providing UNE-loop services (including hot cuts) given the expected retention period of residential customers. Thus, AT&T has not used UNE-loop to provide basic local residential service to customers anywhere in the country. Beyond that, because Verizon and other BOCs have been unable effectively to provision hot-cuts, even in relatively small quantities, in a timely manner and without causing outages for substantial numbers of customers, AT&T generally no longer initially serves even new small business customers with UNE-L. Instead, it initially serves new small business customers through UNE-P – and is seeking to develop procedures in which incumbents will

Competition Provisions in the Telecommunications Act of 1996, Comments of AT&T Corp., Affidavit of C. Michael Pfau, ¶¶ 11-23 CC Docket No. 96-98 (filed May 1999).

¹⁰ See *id.*

¹¹ See *id.*

move large groups of AT&T customers from the incumbent's switch to an AT&T switch on a project basis.¹²

V. UPDATED UNE-P MARGIN ANALYSIS.

21. My initial margin analysis was filed with AT&T's initial comments on December 17, 2001. Since then, I have updated the data used in that margin analysis and implemented improvements to that analysis. The changes to my margin analysis are described below, and full documentation of my analysis is provided in attachments A1-A7.

22. *Feature Revenues.* I have updated the amount of feature revenues that local entrants in Rhode Island can expect to obtain. My initial declaration reflected the then-current penetration rates based on TNS Telecoms TNS ReQuest Market Monitor market research from 1Q01. My updated analysis reflects feature penetration rates from the same source, but based on more recent 3Q01 data. As result of this update, the feature revenues that local entrants in Rhode Island can expect to receive have fallen by \$0.13 to \$3.57. *See Exhibit A-1.*

23. *Usage.* The minutes of use ("MOU") used in my December 2001 margin analysis reflected the projected number of minutes for the year 2001. I have updated that estimate to reflect the projected MOU for the year 2002. In addition, I have fixed an error in the MOU estimate in my margin analysis. The net affect of these two fixes increases the cost of switch usage in my margin analysis by \$0.25/line/month to \$7.14. *See Exhibit A-1, A-5.*¹³

¹² See, e.g., *Performance Measurements and Standards for Unbundled Network Elements and Interconnection*, AT&T Comments, CC Docket No. 01-318, Sczepanski Decl. (filed January 22, 2002).

¹³ The impact of this change on the DUF charge was minimal. With rounding, those costs remained at \$1.07/line/month. *See Exhibit A-1, A-6.*

24. *Access Revenues.* I have also updated my access inputs with third quarter 2001 data. The net result of this change is a decrease in access revenues of \$0.34 to \$1.24. *See* Exhibit A-1, A-7.

25. These changes do not change the basic conclusions made in my December 17, 2001 margin analysis. The state-wide average local residential margins available to new entrants is still negative (with or without the inclusion of intraLATA toll revenues). And the margins available to new entrants in each zone are either negative to small to support entry. Accordingly, local residential entry in Rhode Island is simply not economically feasible.

VI. CONCLUSION

26. For the foregoing reasons, Verizon's criticisms of my Rhode Island margin analyses are baseless, and Verizon's alternative undocumented margin analyses cannot rationally be relied upon to support its application.

VERIFICATION PAGE

I, Michael Lieberman, declare under penalty of perjury that the foregoing is true and correct.

A handwritten signature in black ink, appearing to read "Michael Lieberman", written over a horizontal line.

Michael Lieberman

Executed on February 7, 2002.

Exhibit A-1

Connectivity Margin for Verizon Rhode Island

COSTS		Statewide Average	Zone 1	Zone 2	Zone 3
Zone weights			41%	47%	12%
Loop		\$14.14	\$11.19	\$15.44	\$19.13
Port		\$4.15	\$4.15	\$4.15	\$4.15
Usage		\$7.39	\$7.39	\$7.39	\$7.39
DUF		\$1.07	\$1.07	\$1.07	\$1.07
Platform - Recurring Cost		\$26.75	\$23.80	\$28.05	\$31.74
NRC		\$0.00	\$0.00	\$0.00	\$0.00
Total Platform (w/NRC)		\$26.75	\$23.80	\$28.05	\$31.74
REVENUES		RES @ VZ RI			
Basic Local Svc					
	Zone 1	\$17.26			
	Zone 2	\$15.65			
	Zone 3	\$13.89			
	Basic Local Svc -Statewide	\$16.10			
Other Revenue Sources					
	Features	\$3.57			
	Subscriber Line Charge	\$5.00			
	Access	\$1.24			
Total Revenue					
	Zone 1	\$27.07			
	Zone 2	\$25.47			
	Zone 3	\$23.71			
	Total Revenue -Statewide	\$25.91			
MARGINS - RES @ VZ RI		Level	%		
Zone 1		\$3.28	12%		
Zone 2		(\$2.58)	-10%		
Zone 3		(\$8.03)	-34%		
Residence Statewide		(\$0.83)	-3%		
Connectivity margin					

Exhibit A-2**Rhode Island****UNE-P: Current UNE Rates**

	By Density Zone	Urban	Suburban	Rural	Statewide
A.	Residence Line Distribution	41%	47%	12%	100%
B.	Loop	\$11.19	\$15.44	\$19.13	\$14.14
C.	Analog Line Side Port	\$4.15	\$4.15	\$4.15	\$4.15
D.	Local Switch Usage - Orig				\$0.002921
E.	Local Switch Usage - Term				\$0.002563
F.	Local Switch - Common Trunk Port				\$0.000678
G.	Tandem Switching				\$0.001705
H.	Tandem Switching - trunk port				
I.	Common Transport				\$0.001050
J.	DUF: Per Record Processed				\$0.004099
K.	DUF: Per Record Transmitted				\$0.000118

Exhibit A-3

Residential Toll Conversation MOU Per line Per Month

Average Residential Toll Minutes 4Q00 - 2Q01

Verizon		Rhode Island
Intra-Lata	Intra-State	19.3
	Inter-State	-
Inter-Lata	Intra-State	-
	Inter-State	90.6

Source: TNS ReQuest Market Monitor and Bill Harvesting Study

ARMIS-Based Local DEM Per line Per Month

	2000 Per Line Per Month Local DEM	Total DEM per line CAGR: 2000 vs 1998	Estimated 2002 Per Line Per Month Local DEM
2-Way DEM per Line	1,504	5.2%	1,664
1-Way DEM per Line	752		832

Exhibit A-4

Rhode Island - Verizon Usage Rate Rate Application									
		Local			Intralata toll		Interstate InterLATA		
		interswitch local			On ILEC Network				
		intraswitch local	direct	tandem	intralata toll direct	intralata toll tandem	interlata toll direct	interlata toll tandem	
EO Switching orig	AHD Rates \$ 0.002921	1	1	1	1	1	1	1	
Local Switch - Common Trunk Port	\$ 0.000678		2	2	2	2	1	1	
Common Switched xport	\$ 0.001050		1	2	1	2		1	
Tandem switching usage	\$ 0.001705			1		1		1	
Reciprocal Comp/eo term	\$ 0.003241	1	1	1	1	1			
		\$ 0.006162	\$ 0.008568	\$ 0.011323	\$ 0.008568	\$ 0.011323	\$ 0.003599	\$ 0.006354	
MOU		291	530	11	15	4	145	36	
Cost per Line		\$ 1.79	\$ 4.54	\$ 0.12	\$ 0.13	\$ 0.04	\$ 0.52	\$ 0.23	

MOU Assumptions					
	Outbound	Inbound	total	intraoffice	tandem
Local	832	0	832	35%	2%
IntraLATA Toll	19	0	19	0%	20%
Intrastate InterLATA				0%	20%
Interstate InterLATA	91	91	181	0%	20%
Total	942	91	1033		

Usage Records			
Conversation MOU/MSG		Usage Records	
		Outbound	Inbound
Local	4	208	
IntraLATA Toll	4	5	5
Intrastate InterLATA	4	0	0
Interstate InterLATA	5	18	18
		254	

Usage Cost Per Line

UNE Usage Cost by Service		% MOU	UNE Cost	Average Cost per Line
Local				
	Intrastate local	35%	\$ 0.006162	
	Interstate direct local	64%	\$ 0.008568	
	Interstate tandem local	1%	\$ 0.011323	
			\$ 0.007762	6.46
IntraLATA Toll				
	On ILEC Network			
	intralata toll direct	80%	\$ 0.008568	
	intralata toll tandem	20%	\$ 0.011323	
			\$ 0.009119	0.18
Intrastate InterLATA				
	interlata toll direct	80%	\$ 0.003599	
	interlata toll tandem	20%	\$ 0.006354	
			\$ 0.004150	-
Interstate InterLATA				
	interlata toll direct	80%	\$ 0.003599	
	interlata toll tandem	20%	\$ 0.006354	
			\$ 0.004150	0.75
Total usage cost per line			\$	7.39

VZ Rhode Island_Daily Usage File Calculation

Usage Recording Costs	<u>Rate</u>	<u>Application</u>	<u>Factor</u>		<u>Cost/Month</u>
DUF: Per Record Processed	\$ 0.004099	Per Record	254	Records/Bill	\$ 1.04
DUF: Per Record Transmitted	\$ 0.000118	Per Record	254	Records/Bill	\$ 0.03
Total	\$ 0.004217				\$ 1.07

Lieberman Exhibit 7
Redacted

Basic Local Rates

Access Area	Monthly Line Charge	# of Wire Centers	# of Lines	# of Exchanges
A	\$ 12.30	9	73,250	7
B	\$ 12.94	4	16,897	4
C	\$ 13.26	1	6,641	2
D	\$ 15.62	2	23,005	3
E	\$ 16.65	3	47,166	4
F	\$ 17.26	11	289,588	4
Totals/Avg.	\$ 16.10	30	456,546	24

Source: CCMI

Local Rate effective date 4/8/2001

Features	Expected A la Carte Revenue	Feature Penetration	Feature Rate
Caller ID (Name & Number)	\$1.88	25%	\$ 7.50
Call Waiting	\$1.49	41%	\$ 3.65
Call Forwarding	\$0.21	6%	\$ 3.65
Total	\$3.57		

[Source: TNS Telecoms ReQuest Market Monitor - 3Q01]

Exhibit A-9**Basic Local and UNE Loop Rates by UNE Zone**

UNE Rate		UNE			
Zone	Res Lines	Loop Price	Average Local Rate	# of Wire Centers	
1	188,118	\$ 11.19	\$ 17.26	5	41%
2	212,863	\$ 15.44	\$ 15.65	13	47%
3	55,565	\$ 19.13	\$ 13.89	12	12%
Totals/Avg	456,546	\$ 14.14	\$ 16.10	30	100%

Verizon Rhode Island IntraLATA Toll

Revenue per Switched Line

Year	Rev	Sw Lines (Average)	MTS Rev per Avg SW Line per Mo
1997	34,993	646,885	\$ 4.51
1998	32,156	660,595	\$ 4.06
1999	33,161	670,422	\$ 4.12
2000	27,030	676,363	\$ 3.33

CAGR	-10%
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Source: ARMIS 43-03 and ARMIS 43-08